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NO. _____

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1983

NATALIE KROOG,

Petitioner,

v.

STEVEN MAIT and PAINE, WEBBER, JACKSON & CURTIS,

Respondents.

On Writ of Certiorari
To the United States Court of Appeals
For the Seventh Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether Section 551.59(8) of the Wisconsin Statutes, the anti-waiver provision of the Wisconsin Uniform Securities Law, is preempted by the federal law consisting of the Federal Arbitration Act, the Securities Act of 1933, and the Securities Exchange Act of 1934?

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The petitioner, Natalie Kroog ("Kroog"), prays that a Writ of Certiorari issued to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit, entered in this action on July 15, 1983.

OPINIONS BELOW

The decision and order of the Court of Appeals, dated July 15, 1983, is reported at 712 F.2d 1148, and CCH Federal Securities Law Reporter ¶99,418, and reproduced in the Appendix to this petition, infra, at A-1 et seq.

The decision and order of the United States District Court for the Eastern District of Wisconsin, dated January 7, 1983, is reproduced in the Appendix to this petition, infra, at D-1 et seq.

JURISDICTION

The judgment of the Court of Appeals for the Seventh Circuit was entered on July 15, 1983. A timely petition for rehearing was denied on September 2, 1983, and this petition for certiorari was filed within 90

days of that date. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

STATUTES INVOLVED

Sec. 551.59(8), Wisconsin Statutes:

Any condition, stipulation or provision binding any person acquiring any security to waive compliance with any provision of this Chapter or any rule or order hereunder is void.

Section 551.67, Wisconsin Statutes:

This chapter shall be so construed as to effectuate its general purpose to make uniform the law of those states which enact the "Uniform Securities Act" and coordinate the interpretation and administration of this chapter with related federal regulation.

Section 18, Securities Act of 1933 (15 U.S.C. §77r):

Nothing in this subchapter shall affect the jurisdiction of the securities commission (or any agency or office performing like functions) of any State or Territory of the United States, or the District of Columbia, over any security or any person.

Section 28(a), Securities Exchange Act of 1934 (15 U.S.C. §78bb(a)):

*** Nothing in this title shall affect the jurisdiction of the securities commission (or any agency or office performing like functions) of any State over any security or any person insofar as that it does not conflict with the provisions of this title or the rules and regulations thereunder. ***

Section 14, Securities Act of 1933 (15 U.S.C. §77n):

Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this title or of the rules and regulations of the Commission shall be void.

Section 29(a), Securities Exchange Act of 1934 (15 U.S.C. §78cc(a)):

Any condition, stipulation, or provision binding any person to waive compliance with any provision of this title or of any rule or regulation thereunder, or of any rule of an exchange required thereby shall be void.

Section 2, Federal Arbitration Act (9 U.S.C. §2):

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or trans-

action, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

Section 3, Federal Arbitration Act (9 U.S.C. §3):

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action

until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

STATEMENT OF THE CASE

The Federal Arbitration Act was enacted by Congress in 1925. In 1933 and 1934 Congress enacted the Securities Act and the Securities Exchange Act. In the securities laws, Congress provided that pre-dispute arbitration clauses are not enforceable as to disputes over violations of the securities laws. Section 14 of the Securities Act of 1933 and Section 29(a) of the Securities Exchange Act of 1934. In the securities laws, Congress further provided for concurrent State regulation of securities. Section 18 of the Secur-

ities Act of 1933 and Section 28(a) of the Securities Exchange Act of 1934.

Wisconsin and 36 other states have adopted or substantially adopted the Uniform Securities Act which was drafted by Professor Louis Loss of the Harvard Law School and the National Conference of Commissioners on Uniform State Laws in 1956. Vol. 1, CCH Blue Sky Law Reporter, p. 1503 (Jan. 1982). The uniform law has to be construed to coordinate its interpretation with the Federal Securities Laws (§415, U.S.A. and §551.67, Wis. Stats.). The uniform law provides, like the Federal Securities Laws, that pre-dispute arbitration clauses are not enforceable in disputes over violations of the securities laws [§410, U.S.A. and §551.59(8), Wis. Stats.]. This uniform anti-waiver provision was modeled on the same provision in the Federal Securities

Laws. III Loss, Securities Regulation (1961) at p. 1648.

In Wilko v. Swan, 346 U.S. 427 (1953), this Court held that the anti-waiver statute in the Securities Act of 1933 superseded Section 3 of the Federal Arbitration Act. In Wilko, this Court noted the underlying policy of the securities law anti-waiver provision as being that courts are better equipped to protect investors and implement the securities laws. Prior to this petitioner's case, no court ever held that the Federal Arbitration Act preempted the anti-waiver provision of a state securities law.[1]

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[1] At footnote 3 of the majority opinion in this case, the Court states that the District Court for the Eastern District of Wisconsin twice has held that Section 3 of the Federal Arbitration Act preempted the anti-waiver provision in the Wisconsin Uniform Securities Law. It cites Bache Halsey Stuart Shields, Inc. v. Moebius, 531 F. Supp. 75 (E.D. Wis. 1982) and Barron v. Tastee Freez International, Inc., 482 F. Supp. 1213 (E.D.

In this case the plaintiff sued the defendants in state court alleging claims under the Wisconsin Uniform Securities Law and the common law. The statutory claims pertained to the individual defendant's failing to register as an agent under the Wisconsin Uniform Securities Law, Section 551.31(1), with resulting civil liability under Section 551.59(1). The defendants removed the action to Federal District Court upon the basis of diversity. They then moved under Section 3 of the Federal Arbitration Act to stay proceedings and compel arbitration pursuant to paragraph

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Wis. 1980). Neither case involved that principle of law. Moebius was an employment-termination dispute, wherein the employment contract had an arbitration clause. There was no anti-waiver statute involved, much less the Wisconsin Uniform Securities Law. Barron involved the Wisconsin Franchise Investment Law and not the Wisconsin Uniform Securities Law.

15 of the form Paine, Webber brokerage contract. That paragraph provided for arbitration under the rules of various securities bodies.

The Federal District Court denied the stay as to the plaintiff's statutory claims under the Wisconsin Uniform Securities Law upon the basis that the state law had an anti-waiver provision which was not preempted by federal law. The Federal District Court deemed the relevant federal law to be considered on the question of preemption to be the Federal Arbitration Act and the Federal Securities laws which encouraged concurrent state regulation of securities.

The defendants then appealed to the United States Court of Appeals for the Seventh Circuit. A panel of that Court, in a two-one decision, reversed the District Court's order denying the stay. The Court

of Appeals held that the issue was not whether federal law consisting of the securities laws and the Federal Arbitration Act preempted the state securities law but rather was whether the Federal Arbitration Act alone preempted the state securities law. Within that narrow scope of inquiry, the Court of Appeals held that Section 3 of the Federal Arbitration Act preempted Section 551.59(8) of the Wisconsin Statutes. The dissent agreed with the District Court that the proper scope of inquiry was whether the federal law consisting of the securities laws and the Federal Arbitration Act preempted the Wisconsin Securities Law. The dissent argued that there was no preemption under such an analysis.

REASONS FOR GRANTING THE WRIT

Whether the Anti-Waiver Provision of State Securities Laws is Preempted by the Federal Law is an Important Question of Federal Law which has not been and should be Reviewed by This Court.

This Court currently has under advisement Keating v. Superior Court, Alameda County, 31 Cal. 3d 584, 183 Cal. Rptr. 360, 645 P.2d 1192 (1982), cert. granted sub nom. Southland Corporation v. Keating, No. 82-500 (U.S. Sup. Ct., 1-10-83). The case was argued to the Court on October 4, 1983. Therein, this Court is reviewing the decision of the California Supreme Court that the Federal Arbitration Act does not preempt the anti-waiver provision of the California Franchise Investment Law.

The petitioner's case is far more compeling for a determination of no

preemption, because Keating did not involve a related federal statute, i.e., there are no generalized federal franchise statutes encouraging concurrent state regulation in the franchise area as there are in the securities area.[2] In this case, of course, there are the federal enactments in §18 of the 1933 Act and §28(a) of the 1934 Act providing that the Federal Securities Laws are not to be construed to preempt state regulation. Here, the Court of Appeals, without even considering the Federal Securities Laws, struck down the crucial anti-waiver provision of the state securities laws. The decision effectively bars all investors from bringing civil claims against brokers based on violation

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[2] The Federal Trade Commission has promulgated franchise disclosure rules at 16 C.F.R. §§436.1-.3.

of the state securities laws, since it would take the lantern of Diogenes to locate an investor who would not have signed one of the form brokerage house contracts with a standard arbitration clause.

The Wisconsin Uniform Securities Law was enacted by the Wisconsin legislature pursuant to its inherent police power. Needless to say, Congress has not preempted the area of securities regulation and has encouraged concurrent state regulation. The State of Wisconsin, like 36 other states, has adopted an anti-waiver policy as a part of its securities regulation. In so doing Wisconsin and the other 36 states have adopted the same policy which Congress has deemed to be appropriate in the Federal Securities Laws.

In determining whether Wisconsin ran afoul of federal law by enacting a

duplicate of a federal statute as a part of its concurrent regulation in the area of securities, one should start by reviewing the general principles of preemption. Judge Eschbach of the Seventh Circuit, in his dissent in this case, and the California Supreme Court, in its decision in Keating, looked to this Court's unanimous decision in Merrill Lynch, Pierce, Fenner & Smith v. Ware, 414 U.S. 117 (1973). Therein, this Court held that California's statutory policy excluding wage claims from arbitration was not preempted by New York Stock Exchange arbitration rules promulgated pursuant to federal law. This Court granted certiorari "because of the significance of the question in the area of federal-state relations ...." (414 U.S. at p. 119)

This Court discussed Silver v. New York Stock Exchange, 373 U.S. 341 (1963),

which considered the interrelationship between the federal anti-trust laws and Securities Exchange Act of 1934. This Court then stated:

> "In contrast with Silver, we are not confronted here with conflicting federal regulatory schemes. The present controversy concerns the interrelationship between statutes adopted, respectively, by the Federal Government and a State. *** So here, we may not overlook the body of law relating to the sensitive interrelationship between statutes adopted by the seperate, yet coordinate, federal and state sovereignties. Our analysis is also to be tempered by the conviction that the proper approach is to reconcile 'the operation of both statutory schemes with one another rather than holding one completely ousted.' Id., at 357." (414 U.S. at p. 126)

After reviewing the geneses of the federal law and the state law, this Court stated:

> "Indeed, Congress, in the securities field, has not adopted a regulation scheme wholly apart from and exclusive

> of state regulation. *** 'Where the Government has provided for collaboration the courts should not find conflict.'" (414 U.S. at p. 137)

This Court then concluded its recitation of general principles of preemption by stating as follows:

> "'The principle to be derived from our decisions is that federal regulation of a field of commerce should not be deemed preemptive of state regulatory power in the absence of persuasive reasons - either that the nature of the regulated subject matter permits no other conclusion, or that the Congress has unmistakably so ordained.' Florida Lime & Avocado Growers, Inc. v. Paul, 373 U.S. 132, 142 (1963).
>
> "In other contexts, pre-emption has been measured by whether the state statute frustrates any part of the purpose of the federal legislation. [Citations omitted] ... It is where there is in existence a pervasive and comprehensive scheme of federal regulation that pre-emption follows in order to fulfill the federal statutory purposes." (414 U.S. at p. 139)

Judge Eschbach also relied on New York State Department of Social Services v. Dublino, 413 U.S. 405 (1973). Therein, this Court, after a review of legislative history, arrived at a determination of no preemption because of the inter-relationship between the federal and state laws. The case involved the federal Social Security Act and the WIN rules on the one hand and the State of New York Work Rules as to welfare payments on the other hand. With regard to general principles of preemption, this Court stated as follows:

> "'If Congress is authorized to act in the field, it should manifest its intention clearly. It will not be presumed that a federal statute was intended to supersede the exercise of the power of the state unless there is a clear manifestation of intention to do so. The exercise of federal supremacy is not lightly to be presumed.'" (413 U.S. at p. 413)

and

> "Where coordinated state and federal efforts exist within a complementary administrative frame work, and in the pursuit of common purposes, the case for federal pre-emption becomes a less pursuasive one." (413 U.S. at p. 421)

Contrary to the above well-reasoned passages, the Court of Appeals relied in main part on a portion of Florida Avocado Growers, Inc. v. Paul, 373 U.S. 141 (1963), which had nothing to do with arbitration and wherein this Court stated that the federal law would preempt the state law, if compliance with both would be a physical impossibility. That statement flowed from the following hypothetical by the Court, "That would be the situation here if, for example, the federal orders forbade the picking and marketing of any avocado testing more than 7% oil, while the California test excluded from the State any

avocado measuring less than 8% of oil content." (373 U.S. at p. 143)

It is submitted that the Court of Appeals should have not looked to a decision involving avocado laws but rather should have looked to a unanimous decision involving the federal securities laws and their interrelationship with state laws. It is submitted that federal arbitration will always preempt state anti-waiver statutes, if the Florida Avocado Growers "physical impossibility" test is to be the standard.

Similarly, because this case involves the coordinated federal-state regulation of securities, the cases of Moses H. Cone Memorial Hospital v. Mercury Construction Corp., ____ U.S. ____, 103 S. Ct. 927 (1983) and Prima Paint v. Flood & Conklin Mfg. Co., 388 U.S. 395 (1967), which involved run-of-the-mill commercial

disputes, are of no help in determining the question of preemption. There can be no question that Congress favors arbitration in cases such as those in Moses Cone and Prima Paint.

There also should be no question that Congress does not favor arbitration in the field of securities regulation for all of the reasons articulated in Wilko v. Swan, supra.[3] Indeed, the Seventh Circuit itself agreed with Wilko, when it adopted the position of the Third Circuit that claims under the Securities Exchange Act of 1934

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[3] E.g., "... it is clear that the Securities Act was drafted with an eye on the disadvantages under which buyers labor." (346 U.S. at p. 435) "As the protective provisions of the Securities Act require the exercise of judicial discretion to fairly assure their effectiveness, it seems to us that Congress must have intended §14, note 6, supra, to apply to waiver of judicial trial and review." (346 U.S. at p. 437) See also, Comment, Arbitration of Investor-Broker Disputes, 65 Cal. L. Rev. 120 (1977) at pps. 129-31 for a discussion of the reasons why judicial trial rather than arbitration is crucial to the securities laws.

are not arbitrable and quoted with approval from the Third Circuit as follows:

> "'We need not review here the fundamental and important differences between litigation in a court and arbitration. It is enough to say that the Supreme Court found prospective waivers of the right to judicial trial and review to be inconsistent with Congress' overriding concern for the protection of investors.'" Weissbuch v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 558 F.2d 831, 836 (1977), quoting with approval from Ayres v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 538 F.2d 532, 536, (3rd Cir. 1976), cert. den., 429 U.S. 1010, 97 S. Ct. 542, 50 L.Ed. 2d 619 (1976).

In this case, however, the Seventh Circuit treated this securities matter as if it were a routine commercial dispute and mechanically applied the Federal Arbitration Act to it.

It is submitted that the Court of Appeals' unstudied application of the Federal Arbitration Act, without any consideration of the policies underlying the

Uniform Securities Law of Wisconsin not to mention the other 36 states adopting that law, was in error. It is submitted that a court must always consider the policy underlying the state statute enacted pursuant to the police power, where that statute is part of a complementary federal-state regulation of a field.

It is more particularly submitted that a Court considering federal preemption must look at the policy underlying a state securities law enacted as a part of the Congressionally encouraged state portion of the comprehensive federal-state regulation of the securities field.

Arbitration is and always will be a vehicle of less than universal use. Federal Courts have agreed, for example, that federal antitrust and bankruptcy laws are not arbitrable, because the nature of

the statutory schemes necessitates judicial scrutiny. Allegaert v. Perot, 548 F.2d 432 (2d Cir.), cert. denied, 432 U.S. 910 (1977); American Safety Equipment Corp. v. J.P. Maguire & Co., 391 F.2d 821 (2d Cir. 1968); accord, A. & E. Plastik Pak Co. v. Monsanto Company 396 F.2d 710 (9th Cir. 1968); Lee v. Ply Gem Industries, Inc., 593 F.2d 1266 (D.C. Cir.), cert. denied, 441 U.S. 967 (1979); Applied Digital Technology, Inc. v. Continental Casualty Co., 576 F.2d 116 (7th Cir. 1978). State courts, for futher example, have held that certain claims are not arbitrable due to the nature of the statutory schemes. Kiehne v. Purdy, 309 N.W.2d 60 Minn. (1981) (state securities law claims not arbitrable), Sandefer v. Reynolds Securities Inc., 618 P.2d 690 (Colo. App. 1980) (same); United Nuclear Corp. v. General Atomic Co., 93 N.M. 105, 597 P.2d 290,

cert. denied, 444 U.S. 911 (1979) (state antitrust law claim not arbitrable), Aimcee Wholesale Corp. v. Tomar Products Inc., 21 N.Y.2d 621, 237 N.E.2d 223 (1968) (same); Durst v. Abrash, 22 A.D.2d 39, 253 N.Y.S.2d 351 (1964) (issue of whether transaction was disguised usurious loan not arbitrable).

The securities laws are a golden example of a statutory scheme, where arbitration frustrates rather than promotes the law.

CONCLUSION

Certiorari should be granted to review the decision herein, wherein the Seventh Circuit without any consideration of policies struck a damaging blow to the enforceability of the securities laws of at least 37 states. As stated by the

draftsman of the Uniform Securities Act, "The inadequate budgets and uneven enforcement of the blue sky laws make civil liability the only really effective sanction in many states - perhaps most states." III Loss, Securities Regulation (1961) at p. 1631.

The decision is wholly at odds with the Congressional intent of a complementary federal-state regulation of the securities field and is wholly at odds with the Congressional intent that there be no pre-dispute waivers of the judicial forum in the area of securities regulation. To have a comprehensive federal-state regulation of securities where the state claims are arbitrable and the federal claims are not arbitrable, and where there are all the salutary reasons for not having arbitration in security cases as articulated in Wilko v. Swan, supra, the

effect of the Court of Appeals' decision herein will be to stultify the development of the state portion of the federal-state regulation of securities. All claims will be pleaded under the federal laws. The federal courts will be further encumbered with matters which the state courts are well-equipped to handle. This Court granted certiorari in Keating, supra. With much more reason, it should grant certiorari in this case.

Dated at Milwaukee, Wisconsin, this 1st day of December, 1983.

Respectfully submitted,

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A P P E N D I X

In the

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For the Seventh Circuit

No. 83-1094

NATALIE KROOG,

Plaintiff-Appellee,

v.

STEVEN MAIT and PAINE, WEBBER, JACKSON & CURTIS, INC., a foreign corporation,

Defendants-Appellants.

Appeal from the United States District Court for the Eastern District of Wisconsin.
No. 82 C 363—Robert W. Warren, *Judge.*

ARGUED MAY 13, 1983—DECIDED JULY 15, 1983*

Before WOOD and ESCHBACH, *Circuit Judges*, and CAMPBELL, *Senior District Judge.***

WOOD, *Circuit Judge.* In this appeal, we are called on to decide whether a provision of the Wisconsin Uniform Securities Law which has the effect of negating an otherwise valid arbitration clause in a securities brokerage contract is preempted by Section 3 of the Federal Arbitration Act, 9 U.S.C. § 3, which requires

* An opinion in this case was originally issued as a unanimous opinion on June 14, 1983, but was thereafter withdrawn to permit Judge Eschbach to file a dissenting opinion. The original opinion, now the majority opinion, is unchanged except for the addition of footnotes. Judge Eschbach's dissent has been added.

** The Honorable William J. Campbell, Senior District Judge for the Northern District of Illinois, is sitting by designation.

that "[i]f any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court . . . shall . . . stay the trial of the action until such arbitration has been had . . . ." Because this is a clear case of "actual conflict" between federal and state law as a result of which compliance with both is a "physical impossibility," *Florida Lime and Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 141-43 (1963), we hold, contrary to the district court, that the Arbitration Act must prevail under the Supremacy Clause.

I.

Plaintiff-appellee originally commenced this action in the County Court for Milwaukee County, Wisconsin, seeking to recover losses in her securities brokerage account allegedly caused by defendants-appellees' conduct in violation of the Wisconsin Uniform Securities Law and in violation of the common law. The first cause of action alleged that defendant Mait, as an "agent," bought and sold securities in Wisconsin in violation of the registration requirements contained in the Wisconsin Uniform Securities Law, Wisc. Stat. §§ 551.31(1) and (2), 551.59(1). The second claim alleged that, because Mait was not properly registered, the brokerage contract between the parties was void and subject to rescission. The remaining three causes of action alleged defendants' liability under the common law theories of mismanagement, unsuitable purchases, excessive trading, and breach of fiduciary duty.

Defendants removed the action to federal district court on the basis of diversity. After answering the complaint, defendants moved to stay the proceedings and compel arbitration pursuant to paragraph 15 of the brokerage contract which provided,

> ***Any controversy between us arising out of or relating to this contract or the breach thereof, shall be settled by arbitration*** in accordance with the rules, then obtaining, of either the Arbitration Committee

> of the New York Stock Exchange, American Stock Exchange, National Association of Securities Dealers or where appropriate, Chicago Board Option Exchange or Commodities Futures Trading Commission, as I may elect. I authorize you if I do not make such election, by registered mail addressed to you at your main office within fifteen (15) days after receipt of notification from you requesting such election, to make such election in my behalf. Any arbitration hereunder shall be before at least three arbitrators and *the award of the arbitrators, or of a majority of them, shall be final, and judgment upon the award rendered may be entered in any court, state or federal, having jurisdiction.* (emphasis added).

In further support of their motion to stay, defendants noted the requirements of the Federal Arbitration Act which provide,

> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

9 U.S.C. § 3. Defendants argued that since the controversy at hand arose out of or related to the brokerage contract which was in interstate commerce, and was exactly the kind of dispute the arbitration clause was meant to deal with, the court was required to stay the action and compel arbitration.

Plaintiff opposed the motion to stay, arguing that submission of the dispute to arbitration was forbidden by the Wisconsin Uniform Securities Law, Wisc. Stat. § 551.59(8), which provided, "Any condition, stipulation

or provision binding any person acquiring any security to waive compliance with any provision of this chapter or any rule or order hereunder is void." Submitting the dispute to arbitration, plaintiff argued (and defendants apparently conceded) would effectively deny plaintiff the protection of this non-waiver provision. And Congress, plaintiff argued, could not have intended the commands of the Arbitration Act to overcome such a provision forbidding arbitral waiver of state securities laws. In support of her argument, plaintiff noted that Section 15 of the Federal Securities Act of 1933 specifically forbade waiver of the protection of the Act's provisions, and that this section was subsequently held by the Supreme Court in *Wilko v. Swan*, 346 U.S. 427 (1953), to bar application of Section 3 of the Arbitration Act to stay actions arising under the Federal Securities Act in which the underlying contract contained an arbitration agreement. Plaintiff further argued that since Congress has specifically mandated dual federal-state regulation in the field of securities regulation through Section 18 of the 1933 Securities Act and Section 28(a) of the 1934 Exchange Act and Wisconsin has, pursuant to this authority, enacted an anti-waiver provision nearly identical to the federal provision which was held to eclipse the Arbitration Act in *Wilko*, surely under the pattern of legislative intent discerned in *Wilko*, Congress did not mean the federal Arbitration Act to overcome a state non-waiver provision promulgated pursuant to residual state securities regulation power.[1]

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[1] Plaintiff also apparently argued before the district court that a stay pending arbitration was unwarranted in light of Wisc. Stat. § 551.59(7) which provides that any contract made in violation of the Wisconsin Uniform Securities Law is unenforceable; since the entire brokerage contract at issue was alleged to be unlawful, she argued, the arbitration clause contained therein is also void. Plaintiff appears to have abandoned this alternative argument on appeal, apparently recognizing that it would be unavailing in light of the doctrine announced in *Prima Paint Corp. v. Flood and Conklin Mfg. Co.*, 388 U.S.

(Footnote continued on following page)

The district court agreed with the plaintiff that the Federal Arbitration Act did not require that her first two claims alleging violation of the Wisconsin Securities Law be arbitrated in light of the anti-waiver provision contained in Wisc. Stat. § 551.59(8).[2] The district court began its analysis with the premise that

> [f]ederal regulation of a field must not be deemed preemptive of state regulatory authority in the same field in the absence of good reason. The exercise by a state of its inherent police power, which would be perfectly valid in the absence of federal action, is not preempted unless the intention of Congress to do so is clearly manifested in the federal legislation.

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[1] *continued*
395 (1967), that arbitration clauses are severable, as matter of federal law, from the contracts in which they are embedded and hence allegations as to the unlawful inducement of the contract generally are not sufficient to prevent application of Section 3 of the Arbitration Act. Belatedly on appeal, plaintiff has for the first time sought to exploit the door left open in *Prima Paint*—that contractually prescribed arbitration will not be enforced where there is an allegation of fraud in connection with the making of the agreement to arbitrate, 388 U.S. at 403-04. Although plaintiff on appeal argues that the arbitration clause here, and indeed, any form arbitration clause, is a "fraudulent device," or, alternatively, a contract of adhesion, she cites no record evidence in support of this claim, and the only case she cites in support of this argument is *Wilko v. Swan*, *supra*, which held not that an arbitration clause was *per se* fraudulent, but merely that such a clause conflicted with the policy of the Federal Securities Act. Accordingly, we consider it inappropriate to analyze this belated and unsupported claim on appeal.

[2] The district court did not address whether plaintiff's common law claims could withstand the application of the Federal Arbitration Act, and on appeal, plaintiff has offered no reason why they should not. In light of our holding below with respect to the statutory claims, we will not address this issue but instead instruct the district court on remand to consider whether the common law claims are arbitrable under the contractual arbitration clause here at issue.

The court then posed the issue as a conflict between the mandate of the Arbitration Act and the entire Wisconsin securities regulation scheme, rather than as a conflict between the procedural requirements of the Arbitration Act and the contrary state procedural provision:

> The case at bar presents a state remedial statute which adopts a uniform scheme of economic regulation, enacted pursuant to the state's inherent police power, containing an 'anti-waiver provision.' This state enactment conflicts with a strong federal policy favoring arbitration expressed in the generalized Federal Arbitration Act.

Thus, the district court identified the preemption battlefield involved in this case as that of *securities law* rather than that of policies concerning *informal dispute resolution*:

> . . . the conflict occurs in a subject matter area (securities law) in which the federal enactments contain clear and unequivocal language that they are *not* to be construed so as to preempt state regulation. *See* § 28a 1934 Act, and § 18, 1933 Act.

Having posed this conflict and noting that its own conclusion had been rejected by other district courts,[3] the court here stated its position that

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[3] The conflict presented here has been presented in only three reported federal cases of which we are aware; in all three cases, Section 3 of the Arbitration Act was held to require arbitration despite the presence of a statutory non-waiver provision. *See Bache Halsey Stuart Shields, Inc. v. Moebius*, 531 F. Supp. 75 (E.D. Wis. 1982) (non-waiver provision under Wisconsin Uniform Securities Law); *Barron v. Tastee Freez International, Inc.*, 482 F. Supp. 1213 (E.D. Wis. 1980) (same); *Klein Sleep Products, Inc. v. Hillside Bedding Co.*, Bus. Franch. Guide (CCH) ¶ 7886 (S.D.N.Y. Oct. 13, 1982) (non-waiver provision in New York Franchise Sales Act). However, only in the latter two cases did the court directly discuss the impact of the non-waiver provision.

> because this is a case where the state law involves inherent police power; is remedial in nature; presents a legislatively created cause of action; contains an anti-waiver clause; and deals with an area of the law in which Congress has expressly indicated it has not preempted state regulation, this Court is of the opinion that the statute can withstand the generalized provisions of the Federal Arbitration Act.

Accordingly, the district court denied the defendants' motion to stay proceedings and compel arbitration. From this determination, defendants appeal.

II.

The Supreme Court has mandated that federal preemption questions be addressed through a two-tier inquiry. The reviewing court must first ask whether there is "such actual conflict between the two schemes of regulation that both cannot stand in the same area." *Florida Avocado Growers, Inc. v. Paul*, 373 U.S. 141 (1963). If such "actual conflict" is found, the inquiry is at an end. Or, as the Supreme Court has stated, "A holding of federal exclusion of state law is inescapable and *requires no inquiry into congressional design where compliance with both federal and state regulation is a physical impossibility* for one engaged in interstate commerce. . . ." *Id.* at 142-43. (emphasis added). In short, the assessment of "actual" or "facial" conflict is a threshold inquiry we cannot escape; only if this inquiry is answered negatively can we entertain arguments as to the intent of Congress to occupy the field or preclude the kind of state regulation at issue. *Pacific Gas and Electric Co. v. State Energy Resource Conservation and Development Commission*, ... U.S. ....., 103 S. Ct. 1713, 1722 (1983) ("Even where Congress has not entirely displaced state regulation in a specific area, state law is preempted to the extent that it actually conflicts with federal law."); *Ray v. Atlantic Richfield Co.*, 435 U.S. 151, 158, 165 (1978); *DeCanas v. Bica*, 424 U.S. 351, 363 (1976); *McDermott v. Wisconsin*, 228 U.S. 115 (1913). *See also* L. Tribe, American Con-

stitutional Law, § 6-24 at 377-78 (1978); C. Antieu, 2 Modern Constitutional Law, § 10:22 at 41-42 (1969) ("Where state rules clash with an act of Congress in the field of interstate commerce, there is no weighing by the courts of supposed state interests versus national interests. This the court presumes has been done by Congress in enacting the legislation within its constitutional power.").

The instant case, we think, presents an "actual conflict" which may not be avoided, as the district court endeavored to do, through a balancing of state and federal interests. The Federal Arbitration Act, 9 U.S.C. §3, declares unambiguously that in "*any suit or proceeding* . . . brought in any of the courts of the United States *upon any issue* referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is proceeding *shall* on application of one of the parties *stay the trial of the action until such arbitration has been had* in accordance with the terms of the agreement." (emphasis added). Wisc. Stat. § 551.59(8) purports to prohibit such a procedure. Plainly, here "compliance with both federal and state [laws] is a physical impossibility," *Florida Avocado Growers, Inc. v. Paul*, 373 U.S. 141 (1963). In such circumstances, the Federal Arbitration Act must prevail.

The matter might well stand differently if the Federal Arbitration Act declared only a general, non-binding policy in favor of arbitration, through the use of such qualifying words as "where feasible." But the language of the Act is not precatory. Instead, as the Supreme Court has recently noted, the Act "is a congressional declaration of a liberal federal policy favoring arbitration agreements, *notwithstanding any state substantive or procedural policies to the contrary.* The effect of [Section 2 of the Act, generally holding such agreements enforceable] is to create *a body of federal substantive law* of arbitrability, applicable to any arbitration agreements within the coverage of the Act." *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, ... U.S. ....., 103 S. Ct. 927, 941 (1983) (emphasis added). The Act, then,

clearly mandates a specific procedure "notwithstanding any state substantive or procedural policies to the contrary" upon the meeting of certain prerequisites,[4] the existence of which is not challenged here; the state act blocks the effectuation of that procedure. Thus, the case at bar falls squarely within the line of cases such as *Free v. Bland*, 369 U.S. 663 (1962) (Federal treasury regulations providing that Savings Bonds held in co-ownership pass to a surviving co-owner preempts contrary Texas community property law.); *Castle v. Hayes Freight Lines, Inc.*, 348 U.S. 61 (1954) (Federal certification of motor carrier under Motor Carriers Act preempts state attempt to suspend carriers for violating state highway regulations.); and *McDermott v. Wisconsin*, 228

[4] Plaintiff appears to argue on appeal that the language of Section 2 of the Arbitration Act making arbitration clauses enforceable "save upon such grounds as exist in law or in equity for the revocation of any contract" suggests that Congress countenanced that the Arbitration Act could be voided *ab initio* by state enactments like Wisconsin's purporting to prohibit arbitration. However, this argument, which was not considered by the district court, ignores the language and purpose of the Act. Section 2 by its very terms permits voiding an arbitration clause only on legal grounds applicable to "any contract"; state law aimed specifically at preventing arbitration (unlike, say, the statute of frauds) is obviously not such a universally applicable legal principle. Moreover, such an expansive interpretation of Section 2 is contrary to the entire thrust of the Act which creates a "body of federal substantive law" mandating arbitration "notwithstanding any state substantive or procedural policies to the contrary," *Moses H. Cone Memorial Hospital, supra*, 103 S. Ct. at 941. Although the Supreme Court has not directly addressed this issue, we have previously held that the escape clause of Section 2 makes available only legal and equitable defenses not grounded in state law seeking to directly contravene the federal Act's policies. *Commonwealth Edison Co. v. Gulf Oil Corp.*, 541 F.2d 1263, 1269-70 (7th Cir. 1976). Other circuits have agreed. *See, e.g., Medical Development Corp. v. Industrial Molding Corp.*, 479 F.2d 345, 348 (10th Cir. 1973); *Collins Radio Co. v. Ex-Cell-O Corp.*, 467 F.2d 995, 996-97 (8th Cir. 1972).

U.S. 115 (1913) (Federal act permitting certain labelling preempts contrary state provision preventing use of federally approved labelling.)—all of which held preemption exists where such "actual conflict" between federal and state regulation exists. As surely as Texas community property law prevented federally mandated passage of bond ownership in *Bland* or Illinois law forbade the passage of federally certified carriers in *Castle* or Wisconsin law prohibited the application of federally mandated labels in *McDermott*, the Wisconsin anti-waiver provision as sought to be applied here conflicts with the procedure required under the Federal Arbitration Act. The Wisconsin law may not prevail.

The district court appeared to avoid this result through two-step reasoning. First, it downplayed the existence of direct, irreconcilable conflict (although it did acknowledge that the Wisconsin provision "conflicts" with the Arbitration Act) by maintaining that the real question before it concerned the clash between the Federal Arbitration Act and *the scheme of substantive Wisconsin securities regulation*. Having determined that the Federal Arbitration Act and state securities policy were the contenders for dominance, the district court concluded that the state anti-waiver provision must prevail because Congress declared its intent to leave *state securities regulation* intact and *Wilko v. Swan* expressly approved the confinement of the Arbitration Act where the Federal Securities Act of 1933 was involved (due to the existence of the latter's anti-waiver provision) and thus by analogy would have countenanced the same result where state securities acts were at issue (due to a similar anti-waiver provision). We think the district court's reasoning is vulnerable at either step.

First, the conflict we face is plainly not one of federal arbitration procedures versus Wisconsin substantive securities regulation. The conflict is rather between two *procedural* mandates—one that commands, and the other that prohibits, the arbitration of brokerage contract claims. If the Arbitration Act prevails, Wisconsin substantive securities law remains intact, and would indeed

have to be considered by the arbitrator of the dispute here. In short, the real field of analysis here is the set of competing federal and state policies with respect to *non-legal dispute resolution*, not with respect to *securities regulation*. Accordingly, the district court's citation to the dual federal-state regulatory scheme in the securities field and the Supreme Court's interpretation of the "intention of Congress concerning the sale of securities" in *Wilko v. Swan*, 346 U.S. at 427, 438, is essentially irrelevant to the required analysis.

But even if securities regulation were somehow the field in which the required preemption analysis were to take place, it would still be inappropriate to apply the policy of *Wilko* to constrict the application of the Arbitration Act to claims based on breaches of state securities law. This is so because the Supreme Court in *Wilko* was concerned solely and expressly with the proper reconciliation of two "not easily reconcilable" *federal* mandates—the Securities Act and the Arbitration Act, *see* 346 U.S. at 438. It is a *non sequitur* to assume, as does plaintiff, that this *lateral* balance of diametrically opposed *federal* policies, and consequent delimitation of the Arbitration Act, would be applied vertically to restrict the Arbitration Act's impact on conflicting *state* procedures. To the contrary, to the extent that the Supreme Court held that a Wisconsin-style federal nonwaiver provision and the Arbitration Act were in *direct conflict*, 346 U.S. at 433, 438, its *Wilko* opinion suggests that the Wisconsin procedural provision would have to yield under the "actual conflict" and "physical impossibility" standards enunciated in *Florida Avocado Growers, Inc. v. Paul*, 373 U.S. 141 (1963), and its predecessors and progeny. To hold that *Wilko*'s delimitation of the Arbitration Act's application to another federal law is vertically transferable to protect state anti-waiver clauses is to deny that Congress may choose not to apply interstate commerce-based policies to exclusively Federal subject matter. Such a view cannot be correct, for it is unquestioned that Congress has the power to, and regularly does, exempt exclusively federal

subject matter from the reach of substantive interstate commerce regulation (*e.g.*, in the nuclear power and environmental fields) without thereby automatically sanctioning state attempts to remove private and state actors from such regulation.[5]

In sum, we think that the district court's search for congressional intent with respect to the Arbitration Act *via* the 1933 and 1934 Securities Acts and *Wilko* could not be productive. Here we face a naked and irreconcilable conflict between a precise federal mandate to arbitrate and a state provision which prevents arbitration. Once that conflict has been described, we need go no further, for federal preemption in such cases is automatic. *Pacific Gas and Electric Co.*, ... U.S. ....., 103 S. Ct. 1713 (1983); *Ray v. Atlantic Richfield Co.*, 435 U.S. 151, 158, 165 (1978).

For the foregoing reasons, the district court's denial of defendants-appellants' motion to stay proceedings and compel arbitration is reversed and the case is remanded with directions that proceedings be stayed and plaintiff-appellee's statutory claims, and, if otherwise warranted, her common law claims, be submitted to arbitration.

REVERSED AND REMANDED.

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[5] It is true, as the dissent notes, that the case for federal preemption may be less persuasive where coordinated state and federal efforts exist within a complimentary administrative framework. *New York State Department of Social Services v. Dublino*, 413 U.S. 405, 421 (1973). But here there is no indication that Congress has chosen to temper the imperatives of the Federal Arbitration Act with respect for *state* policies regarding informal dispute resolution in the securities, or any other, field. *Compare Dublino, supra*, at 418-21 (no preemption found where federal statute contains express statement of its limited applicability against states and where there exists long-standing federal administrative practice of deferring to state activity).

ESCHBACH, *Circuit Judge*, dissenting. While I agree with many of the general principles discussed in my brother Wood's well written opinion, I part company with the majority on an issue of critical importance—the content of the federal law which is to be compared with the Wisconsin anti-waiver provision in order to determine whether federal law has preempted state law. The majority compares the provisions of the Federal Arbitration Act with the provisions of the Wisconsin Uniform Securities Law and concludes that there is an actual or facial conflict. With this I agree. However, in assessing whether "federal law" has preempted the Wisconsin anti-waiver provision, we must look not only at the Federal Arbitration Act, but also at other federal laws and court decisions that have interpreted, applied, and possibly modified the Arbitration Act. *See Jones v. Rath Packing Co.*, 430 U.S. 519, 526 (1977) (court must consider relationship between state and federal laws as they are interpreted and applied, not just as they are written). The relevant federal law in this case consists of the Federal Arbitration Act, the federal securities acts of 1933 and 1934, and case law interpreting these statutes.

Section 18 of the Securities Act of 1933, 15 U.S.C. § 77n, and § 28(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78bb(a), specifically provide for concurrent state regulation of securities. Section 14 of the 1933 Act, 15 U.S.C. § 77n, bars waiver of a judicial forum by an arbitration agreement, in spite of the provisions of the Federal Arbitration Act favoring such agreements. *Wilko v. Swan*, 346 U.S. 427, 438 (1953). While *Wilko* dealt only with actions under the federal securities laws, much of the court's analysis applies with equal force to a state's attempt to preserve a judicial forum for buyers of securities. The Court enumerated possible shortcomings of arbitration in this field and recognized that the advantages the securities laws provided a buyer may be less effective in arbitration than in judicial proceedings. *Id.* at 434-37. The Court found it reasonable for Congress to put buyers of securities covered by the 1933 Act on a different basis from other

purchasers. *Id.* at 435. From the provisions of the federal securities acts specifically sanctioning state regulation and from the Supreme Court's interpretation of the acts in *Wilko*, I conclude that Congress, in enacting the securities acts, impliedly modified the preexisting general provisions of the Arbitration Act as they would apply in the areas of both federal and state securities regulation. Thus, while the bare words of the Arbitration Act are in facial conflict with the Wisconsin Uniform Securities Law, "federal law" is not.

Having answered the threshold question of actual or facial conflict in the negative, I find that the district court was correct in its analysis of the competing federal and state interests and in its conclusion that the Wisconsin anti-waiver provision has not been preempted by federal law. Contrary to the majority's assertion, the "preemption battlefield" in the instant case is not merely that of policies concerning informal dispute resolution, but rather that of procedural advantages necessary to fully effectuate the substantive provisions of the Wisconsin securities laws. *Cf. id.* at 434-37 (discussing the advantages of a judicial forum over arbitration in the context of federal securities laws). Wisconsin has chosen to regulate securities in a framework that is complementary to federal law and which furthers a common purpose, i.e., the protection of the investor. In this situation, the case for preemption is not persuasive. *See New York State Department of Social Services v. Dublino*, 413 U.S. 405, 421 (1973); *cf. Merrill Lynch, Pierce, Fenner & Smith v. Ware*, 414 U.S. 117, 137 (1973) (where the federal government provides for collaboration, the courts should not find conflict). In support of my conclusion that federal law has not preempted the Wisconsin anti-waiver provision, I concur in the following analysis of the district court:

> Proper adherence to the principles of Federalism require that, where there is a conflict between state and federal policies, preemption of the subject area by the federal enactment should take place only when Congress clearly intends it to occur. The case at bar presents a state remedial statute which

adopts a uniform scheme of economic regulation, enacted pursuant to the state's inherent police power, containing an "anti-waiver" provision. This state enactment conflicts with a strong federal policy favoring arbitration expressed in the generalized Federal Arbitration Act. However, the conflict occurs in a subject matter area (securities law) in which the federal enactments contain clear and unequivocal language that they are *not* to be construed so as to preempt state securities regulation. *See* § 28a, 1934 Act, and § 18, 1933 Act. In this context, it would seem that the Arbitration Act ought not to preempt the Wisconsin Securities law with its anti-waiver provision.

* * *

In summary, because this is a case where the state law involves inherent police power; is remedial in nature; presents a legislatively created cause of action; contains an anti-waiver clause; and deals with an area of the law in which Congress has expressly indicated it has not preempted state regulation, this Court is of the opinion that the statute can withstand the generalized provisions of the Federal Arbitration Act.

Decision and Order at 8, 11. Kroog should not be compelled to arbitrate the two claims she brought under the Wisconsin Uniform Securities Law. Accordingly, I respectfully dissent from the majority's decision directing that proceedings be stayed pending arbitration of these claims.

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Opinion by Judge Wood
Judge Eschbach dissenting

JUDGMENT - ORAL ARGUMENT

UNITED STATES COURT OF APPEALS
For the Seventh Circuit
Chicago, Illinois 60604

July 15, 1983

Before

Hon. HARLINGTON WOOD, JR., Circuit Judge
Hon. JESSE E. ESCHBACH, Circuit Judge
Hon. WILLIAM J. CAMPBELL, Senior District Judge*

NATALIE KROOG, Plaintiff-Appellee, No. 83-1094 vs. STEVEN MAIT & PAINE, WEBBER, JACKSON & CURTIS, INC., a foreign corporation, Defendants-Appellants.	Appeal from the United States District Court for the Eastern District of Wisconsin No. 82 C 0363 Judge Robert W. Warren

This cause was heard on the record from the United States District Court for the Eastern District of Wisconsin, Division, and was argued by counsel.

On consideration whereof, IT IS ORDERED AND ADJUDGED by this Court that the

judgment of the said District Court in this cause appealed from be, and the same hereby, REVERSED, with costs, and the case is REMANDED, with directions, in accordance with the opinion of this Court filed this date.

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* The Honorable William J. Campbell, Senior District Judge for the Northern District of Illinois, is sitting by designation.

UNITED STATES COURT OF APPEALS
For the Seventh Circuit
Chicago, Illinois 60604

September 2, 1983

Before

Hon. HARLINGTON WOOD, JR., Circuit Judge
Hon. JESSE ESCHBACH, Circuit Judge
Hon. WILLIAM J. CAMPBELL, Senior District Judge*

NATALIE KROOG,
Plaintiff-Appellee,

No. 83-1094 vs.

STEVEN MAIT & PAINE, WEBBER, JACKSON & CURTIS, INC., a foreign corporation,
Defendants-Appellants.

Appeal from the United States District Court for the Eastern District of Wisconsin
No. 82 C 0363
Judge Robert W. Warren

ORDER

On consideration of the petition for rehearing and suggestion for rehearing in banc filed in the above-entitled cause by cousnel for plaintiff-appellee, no judge in active service has requested a vote thereon, and all of the judges on the original panel have voted to deny a rehearing. Accordingly,

IT IS ORDERED that the aforesaid petition for rehearing be, and the same is hereby, DENIED.

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* The Honorable William J. Campbell, Senior District Judge for the Northern District of Illinois, is sitting by designation.

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF WISCONSIN

NATALIE KROOG,

Plaintiff,

vs. Case No. 82-C-0363

STEVEN MAIT and PAINE, WEBBER, JACKSON & CURTIS, INC., a foreign corporation,

Defendants.

DECISION AND ORDER

This action was commenced in February 1982 in Milwaukee County Circuit Court. The complaint sets forth five separate causes of action in which plaintiff alleges that the defendants are liable for losses in her brokerage account amounting to $82,006.69 plus commission and interest charges. The first cause of action alleges that defendant Mait, as "agent," bought and sold securities in Wisconsin in violation of registration requirements contained in sections 551.31(1) and (2) as well as section 551.59(1) of the

Wisconsin Uniform Securities Law. The second claim alleges that, because Mait was not properly registered, the investment contract between the parties is void and subject to recission. The other three claims allege liability based on mismanagement, unsuitable purchases, excessive trading, and breach of fiduciary duty.

Defendants removed the case to this Court based on diversity. Defendants sought arbitration under paragraph 15 of the brokerage contract (Exhibit A attached to Affidavit of Robert L. Salzberg) and thereafter filed their answer. They have now moved this Court to stay proceedings and compel arbitration.

The Wisconsin Commissioner of Securities sought and obtained leave to file a brief amicus curiae.

Defendants argue that arbitration should be compelled because paragraph 15 of the Client Agreement provides:

> Any controversy between us arising out of or relating to this contract or the breach thereof, shall be settled by arbitration in accordance with the rules, then obtaining, of either the Arbitration Committee of the New York Stock Exchange, American Stock Exchange, National Association of Securities Dealers or where appropriate, Chicago Board Option Exchange or Commodities Futures Trading Commission, as I may elect. I authorize you if I do not make such election, by registered mail addressed to you at your main office within fifteen (15) days after receipt of notification from you requesting such election, to make such election in my behalf. Any arbitration hereunder shall be before at least three arbitrators and the award of the arbitrators, or of a majority of them, shall be final, and judgment upon the award rendered may be entered in any court, state or federal, having jurisdiction. (Emphasis added).

The Federal Arbitration Act, 9 U.S.C. § 1 et. seq, establishing a strong federal policy favoring arbitration as a dispute-settling mechanism, provides:

> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding

> is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

9 U.S.C. § 3.

Defendants contend that under the arbitration agreement, the present controversy arises out of or relates to the contract or breach thereof; that the transaction involved a contract in interstate commerce such that the Arbitration Act applies; and that, given the fact that the dispute arises directly out of the management of plaintiff's brokerage account and is exactly the kind of dispute the arbitration clause is meant to deal with, the Court should stay this action and compel arbitration. 9 U.S.C. §§ 2 and 3.

Plaintiff contends that an exception to the policy considerations favoring arbitration exists where the claims are based on a "statutory enactment promulgated for the protection of the public welfare"

and cites cases involving specific remedial acts dealing with such subjects as labor standards, patent validity, usury, and pension protection. Wilko v. Swan, 346 U.S. 427 (1953), wherein a private action based on the Federal Securities Act of 1933 was held not arbitrable despite the inclusion of an arbitration clause in the brokerage agreement, the plaintiff points to the Supreme Court's statement in the case that:

> § 14, note 6 of the 1933 Act voids any stipulation waiving compliance with the provisions of the Securities Act. This arrangement to arbitrate is a "stipulation" and we think the right to select a judicial forum is the kind of "provision" that cannot be waived under § 14 of the Securities Act.

Id. at 434-435.

Plaintiff further argues that such reasoning was adopted by the Seventh Circuit in Weissbuch v. Merrill Lynch, Pierce, Fenner & Smith, 558 F.2d 831 (7th Cir. 1977), and that a similar line

of reasoning should apply to the Wisconsin Uniform Securities Act, which contains a non-waiver provision comparable to that in Section 14 of the federal act.

As an ancillary argument, plaintiffs contend that defendant Mait's activities caused the contract containing the arbitration agreement to be void. Section 551.59(7) Wis. Statutes recites that:

> No person who has made or engaged in the performance of any contract in violation of this chapter or any rule or order hereunder, or who has acquired any purported right under any contract with knowledge of the facts by reason of its making or performance was in violation, may base any suit on the contract.

Hence, it is argued, any effort by defendants to enforce the arbitration clause is to no avail since the contract itself is, under Wisconsin law, void pursuant to section 551.59(7).

The Commissioner's amicus brief notes that Chapter 551, Wis. Stats., is almost a verbatim adoption of the uniform act adopted

by the National Conference of Commissioners on Uniform State Laws. It further notes that section 14 was drafted and adopted to encompass the holding of Wilko v. Swan, supra, and to make § 551.59(8), Wis. Stats., bar pre-dispute waiver of state securities laws in a fashion parallel to the Wilko doctrine at the federal level. Plaintiff and the Commissioner argue that the public policy factors are the same in each arena -- the federal and the state -- and that the enforcement scheme is the same with anti-waiver provisions in each law so as to equalize the knowledge position of the contracting parties. The theory here is that the typical contracting investor would not be aware that in signing a brokerage contract he was agreeing to arbitration and waiving the protection of the remedial securities law involved -- either federal or state. Plaintiffs contend that preemption of §§ 551.59(7) and (8), Wis. Stats., by the

Federal Arbitration Act will force investors into arbitration and deny them many rights solely because the claims arise under state securities law and not under comparable provisions of the federal securities laws where the Wilko doctrine would prevent such injustice.

For analytical purposes, one must start with the basic premise that, under the Tenth Amendment, those powers not granted to the federal government are reserved to the states or to the people. To be sure, the "powers" of the Congress under the commerce and welfare clauses have been rather limitlessly construed by the courts such that preemption is possible in a wide range of areas. Under the Supremacy Clause such enactments become the law of the land. Nonetheless, there is discernible reluctance to interfere with the police power of the sovereign states, and properly so. Federal regulation of a field must not be deemed preemptive of state

regulatory authority in the same field in the absence of good reason. The exercise by a state of its inherent police power, which would be perfectly valid in the absence of federal action, is not preempted unless the intention of Congress to do so is clearly manifested in the federal legislation. International Union United Auto Workers, A.F. of L., Local 232 v. Wisconsin Employment Relations Board, 336 U.S. 245 (1949). In its legislative enactments, Congress is prone to make clear whether or not a given act is intended to exist in tandem with state pronouncements in the area, or whether the federal action is to preempt the area entirely.

There is no such clear mandate with reference to the Federal Arbitration Act, and when the application of the Act becomes intertwined with various federal remedial programs, the waters become murky indeed. The amicus brief traces the

history of the Federal Arbitration Act from its enactment in 1925. Its purpose was to make agreements for arbitration as effective and enforceable as any other contracts. American Airlines, Inc. v. Louisville & Jefferson County Air Board, 269 F.2d 811, 815 (6th Cir. 1959).

In 1959, the Second Circuit, in Lawrence Company v. Devonshire Fabrics, Inc., 271 F.2d 402 (2nd Cir. 1959), held that the Act created a new body of federal "substantive law" resting on Congress' power to regulate interstate commerce. This led a number of courts to the conclusion that the Federal Arbitration Act could require arbitration despite the doctrine of Erie Railway Co. v. Tompkins, 304 U.S. 64 (1938). See Metro Industrial Plating Corp. v. Terminal Construction Co., 287 F.2d 382 (2nd Cir. 1962); Prima Paint Corp. v. Flood and Conklin Mfg. Co., 388 U.S. 395 (1967).

The Court has considerable doubt as to the efficacy of such reasoning. It would seem a rather superficial solution to the problem to simply call the Federal Arbitration Act "substantive law" and apply it to diversity cases without further analysis. It is more appropriate to consider the nature of the contending powers and policies--and decide accordingly.

Proper adherence to the principles of Federalism require that, where there is a conflict between state and federal policies, preemption of the subject area by the federal enactment should take place only when Congress clearly intends it to occur. The case at bar presents a state remedial statute which adopts a uniform scheme of economic regulation, enacted pursuant to the state's inherent police power, containing an "anti-waiver" provision. This state enactment conflicts with a strong federal policy favoring arbitration expressed in the

generalized Federal Arbitration Act. However, the conflict occurs in a subject matter area (securities law) in which the federal enactments contain clear and unequivocal language that they are not to be construed so as to preempt state securities regulation. See § 28a 1934 Act, and § 18, 1933 Act. In this context, it would seem that the Arbitration Act ought not to preempt the Wisconsin Securities law with its anti-waiver provision.

In making this decision, the Court is very much aware that it is in apparent conflict with a number of district court decisions by its colleagues here in the Eastern District of Wisconsin.

Judge Reynolds, in Romnes v. Bache & Co., 439 F.Supp. 833 (E.D. Wis. 1977), dealt with a similar problem. There, plaintiffs sued the broker for alleged violations of the Commodities Exchange Act, the Wisconsin Uniform Securities Act, and the common

law regarding brokerage accounts. Defendants sought a stay and arbitration. Judge Reynolds held that, under federal law, a trading account in commodities futures is not a "security." Thus, the case turned upon the application of the Commodities Exchange Act. Since that Act had no "anti-waiver" provisions, and the Arbitration Act was deemed substantive law, the controversy was determined to be arbitrable. The Court stated:

> The Federal Arbitration Act, 9 U.S.C. § 1 et seq., creates federal substantive law under the authority of the Interstate Commerce Clause. It is not merely procedural. Therefore it requires a federal court to adjudicate the issue of the enforceability of an arbitration clause even in a diversity action according to federal law. Federal court is not bound under the doctrine of Erie Railroad Co. v. Thompkins, supra.

493 F.Supp. at 838. The absence of any anti-waiver provision in the Commodities Exchange Act leads to the conclusion that case presented a different proposition than the case at bar.[1]

Judge Reynolds looked to his earlier Romnes decision when faced with a similar dilemma in Barron v. Tastee Freez International, Inc., 482 F.Supp. 1213 (E.D. Wis. 1980). There the question was whether arbitration should occur when some of the claims were for various violations of the Wisconsin and Illinois Franchise Investment Acts, which each contained anti-waiver provisions. Judge Reynolds apparently felt that the effect of the Federal Arbitration Act upon the anti-waiver clause of remedial legislation had been settled by Romnes -- perhaps on the basis of Lawrence Company v. Devonshire Fabrics, supra, which he quoted in the Romnes opinion.

Plaintiffs contend that the Barron case was inadequately briefed and argued to the court; that the impact of the Federal Arbitration Act upon state police-power statutes was never discussed, but only the effect on state common law and state

arbitration statutes per se; and that during the proceedings, Judge Reynolds had been under the mistaken impression that Romnes dealt with "the Uniform Securities Act" (Barron transcript, p. 19.)

In Bache Halsey Stuart Shields, Inc. v. Moebius, 531 F.Supp. 75 (E.D. Wis. 1982). Judge Gordon had occasion to consider the Federal Arbitration Act and cited Barron for the Act's supremacy over state law. But in Moebius, the factors of an anti-waiver provision and the absence or presence of a statement of Congressional intent as to preemption were not before the court.[2]

In summary, because this is a case where the state law involves inherent police power; is remedial in nature; presents a legislatively created cause of action; contains an anti-waiver clause; and deals with an area of the law in which Congress has expressly indicated it has not preempted state regulation, this Court is of the

opinion that the statute can withstand the generalized provisions of the Federal Arbitration Act.

Therefore, the motion of defendants to stay proceedings and compel arbitration is herewith DENIED.

SO ORDERED this 7th day of January 1983, at Milwaukee, Wisconsin.

ROBERT W. WARREN
UNITED STATES DISTRICT JUDGE

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[1]It is to be noted in passing that the Commodities Exchange Act had no legislatively created right of action for damages such as the federal securities laws and the Wisconsin act have.

[2]The cases of Allison v. Medicab International Inc., 92 Wash.2d 199, 597 P.2d 380 (1979) and Keating v. Superior Court, Alameda County, 167 Ca. Reptr. 481 (Cal. App. 1980), which defendants cite in their reply brief are state cases and are not persuasive in light of the policy considerations set forth herein.